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89-1898

CAUSE NO.

In The

United States Supreme Court

OCTOBER 1989 TERM

BELL & MURPHY AND ASSOCIATES, INC.,
JOHN W. BELL, JR., HAROLD D. BARNETT,
ROBERT D. HAMER, JR., AND RICHARD L. MEARS,
PETITIONERS,

VS

FEDERAL DEPOSIT INSURANCE CORPORATION, AS
RECEIVER FOR FIRST REPUBLICBANK DALLAS, N.A.
(F/K/A FIRST REPUBLICBANK GATEWAY, N.A.),
NCNB TEXAS NATIONAL BANK, N.A., AND
CHARLES E. JOBE,
Respondents.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

PETITION FOR WRIT OF CERTIORARI

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QESTIONS FOR REVIEW

1. Does the common law doctrine of *D'Oench, Duhme & Co., v. FDIC,* 315 U.S. 447 (1942) bar Petitioners' causes of action against the FDIC?

2. Does the fact that the agreement was in writing in the form of a letter from the Bank take it out of the purview of *D'Oench?*

3. Is the *D'Oench* doctrine limited to agreements which diminish the FDIC's interest in a specific asset acquired from a bank?

4. Does *D'Oench* require a showing of some sort of fault on the part of the party opposing the FDIC?

5. Are the lower court's rulings on questions 3. and 4. above supported by precedent?

6. Does the fact that the agreement established on its face bilateral obligations take it out of the purview of *D'Oench?*

LIST OF PARTIES

All parties are listed in the caption of this petition.

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REFERENCE TO APPELLATE COURT'S OPINION

The Fifth Circuit did publish an opinion in this case which appears at 868 F.2d 750 and is appended hereto.

STATEMENT OF JURISDICTION

On February 21, 1990, the Fifth Circuit Court of Appeals issued and entered judgment affirming the judgment of the trial court in this litigation. This Petition is presented to this Court pursuant to 28 U.S.C. Sec. 1254 (1).

CITATION OF RELEVANT STATUTE

Although not controlling, 12 U.S.C. Sec. 1823(e) is relevant to the issues in this petition. The statute is set out below.

> No agreement which tends to diminish or defeat the right, title or interest of the Corporation in any asset acquired by it under this section, either as security for a loan or by purchase, shall be valid against the Corporation unless such agreement (1) shall be in writing, (2) shall have been executed by the bank and the person or persons claiming an adverse interest thereunder, including the obligor, contemporaneously with the acquisition of the asset by the bank, (3) shall have been approved by the board of directors of the bank or its loan committee, which approval shall be reflected in the minutes of said board or committee, and (4) shall have been, continuously, from the time of its execution, an official record of the bank.

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STATEMENT OF THE CASE

A. *Course of proceedings*

This case originated in the courts of the State of Texas. Bell & Murphy and Associates and the individual Petitioners (collectively hereinafter "Petitioners") filed suit in the 352d District Court of Tarrant County, Texas. The defendants to the suit were originally Interfirst Bank Gateway, N.A. and its president, Charles E. Jobe. Subsequently,

Interfirst bank became First Republicbank Gateway, N.A., and then the First Republicbank system failed. The FDIC became receiver of the failed bank, and NCNB Texas National Bank acquired First Republicbank. Due to this course of events, FDIC and NCNB became parties to this litigation.

FDIC then sought removal of the suit to the United States District Court for the Northern District of Texas, Fort Worth Division. The removal petition was amended to include Jobe, and eventually the removal petition was granted.

FDIC and NCNB next moved for dismissal for failure to state a claim. The motion was based on *D'Oench, supra,* and 12 U.S.C. Sec. 1823(e). The District Court granted the motion.

Petitioners appealed that decision to the Fifth Circuit, which upheld the trial court's judgment.

B. *Statement of facts*

The facts which form the basis of this suit appear below. Many of these facts are allegations in Petitioners' Original Petition; however, since the case was dismissed for failure to state a claim, these allegations must be accepted as true. *Jenkins v. McKeithen,* 395 U.S. 411, 421-422 (1969).

The Court should be aware that several different bank names are involved, but regardless of what names are applicable at what times, there is but one bank which engaged in the conduct which is the basis of the suit. Therefore, in order to avoid confusion, this petition will henceforth refer to "Bank" unless it is necessary to use a specific name.

The facts are as follows. Petitioners' business involved consultation and exploration in oil and gas. Due to the

nature of the Texas economy and the oil and gas industry, Petitioners began experiencing substantial financial difficulties in 1985.

At that time, Petitioners had a seventeen-year history of doing business at the Bank. Petitioners sought assistance from the Bank, and the parties reached an agreement. That agreement is not the basis of this suit. The agreement was nonetheless breached by the Bank.

The Bank demanded a new agreement, and Petitioners, given their condition and actions in reliance of the initial agreement, had no choice but to accept the Bank's demands. This new "agreement" was accepted by Petitioners under economic duress.

After the revised agreement became effective, the Bank demanded additional terms. Again, Petitioners were forced to comply with these new terms under economic duress.

The terms of the agreement were as follows. Petitioners' accounts receivable would be paid to the Bank. Petitioners would obtain loans from their pension and profit sharing plans, and these funds would then be loaned to Bell & Murphy and Associates (hereinafter "BMA"). BMA would in turn give these funds to the Bank. Two-thirds of these funds would be retained by the Bank and applied to BMA's outstanding debt with the Bank. The other one-third would go to the IRS for back payroll taxes. BMA would change its pay period to semi-monthly and reduce pay of all officers and other employees. In return, the Bank was to honor checking overdrafts for payroll checks, checks to the IRS, and checks for necessary operating expenses. These overdrafts were essentially covered in that the Bank had possession of all of BMA's accounts receivables. Also, BMA was to have been able to operate without limitation. The Bank was

obligated to work with BMA as long as Petitioners complied with the agreement.

The above agreement was in writing in the form of a letter from Jobe.

Petitioners complied with all the terms of the agreement; however, the bank breached the agreement. The Bank in effect used all of the money from the pension and profit sharing plans and the accounts receivable only to reduce Petitioners' indebtedness to the Bank as quickly as possible. Such action was taken in total disregard to whether BMA survived as a business.

The Bank's misrepresentations, mismanagement, and breach of the agreement effectively destroyed Petitioners' business.

The only asset of the Bank that was involved and could have been affected in any way by the agreement was Petitioners' outstanding indebtedness to the Bank. The Petitioners' pension and profit sharing plans had no connection to the Bank. Also, Petitioners have never sought to avoid any obligation to the Bank.

ARGUMENT

I. *REASONS FOR ALLOWANCE OF WRIT*

The lower court's rulings conflict with rulings from other Circuits regarding the following issues: 1) whether *D'Oench* applies only to agreements adversely affecting the FDIC's interest in specific assets acquired from a bank, and 2) whether *D'Oench* requires a showing of some sort of fault on the part of the party opposing the FDIC.

The above issues have not been settled by this Court, and Petitioners urge that they are important issues of federal

law which should be settled by this Court, particularly given the conflicts among the Circuit courts.

Petitioners further maintain that the appellate court's ruling on the "specific asset" issue is unsupported by precedent, and thus constitutes an unjustified and incorrect expansion of the *D'Oench* doctrine. Petitioners feel this Court should review such decision before allowing a lower court to create new law which might be in conflict with existing law.

The concerns expressed in the previous paragraph also apply to the appellate court's ruling on the fault issue.

The above reasons for allowing the writ are explained in detail below.

II. *SUMMARY OF SELECTED CASE LAW*

Petitioners have summarized cases which are pertinent to this cause. Many of these cases are the more prominent and most often cited cases regarding D'Oench and its statutory counterpart. Petitioners do not represent that their list of summaries is conclusive; however, they have made a good faith effort to find cases which address the issues raised herein, and they are not purposely omitting cases which do not support their arguments.

These summaries are intended to serve as a ready aid in analyzing Petitioners' arguments. Many of the cases are applicable to several different issues herein, and rather than explain the circumstances of a given case several times, Petitioners felt the requirements of brevity and conciseness would be better serve by summarizing the cases here and simply referring to those cases in the Argument.

Langley v. FDIC, 108 S. Ct. 396 (1987).

This decision was based on 12 U.S.C. Sec. 1823(e), but this Court relied on *D'Oench* in interpreting the statute.

The pertinent facts were 1) the Langleys signed facially unqualified promissory notes, 2) the FDIC attempted to enforce the notes, 3) the Langleys claimed the notes were invalid due to fraud in the inducement, and 4) such alleged fraud served as the basis for a counterclaim.

This Court rejected the Langleys' fraud claims on the basis of *D'Oench.* This Court found that the alleged misrepresentations and subsequent execution of the notes constituted a "scheme or arrangement" under *D'Oench. Id.* at 402. The Court stated:

> Certainly, one who signs a facially unqualified note subject to an unwritten and unrecorded condition upon its repayment has lent himself to a scheme or arrangement that is likely to mislead the banking authorities, whether the condition consists of performance of a counterpromise (as in *D'Oench, Dunme*) or of the truthfulness of a warranted fact. *Id.*

Petitioners submit that the Langleys' claims, including the counterclaim, were barred because their "agreement" would alter the plain terms of their obligation. Regarding the counterclaim, Petitioners point out that it was based on an agreement, which if allowed, would have adversely affected a specific asset.

FDIC v. Powers, 576 F. Supp. 1167 (N.D. Ill. 1983).

The impact of this case is shown in two excerpts from the opinion. The first excerpt states:

> The FDIC sues Powers on a facially sufficient guarantee, and he wishes to defend on the basis of informal, unwritten arrangements and understandings between him and [bank] officials. *Id.* at 1171.

Powers signed the guarantee in blank, and he claimed that there was no agreement to use the instrument to guarantee the debt in issue. *Id.* at 1169. This defense was held barred. *Id.* at 1171.

The "understanding" was that the blank guarantee was not to be used to secure the debt in issue. Just as was the case in Langley, the unrecorded "agreement" sought to alter the plain terms of a written obligation, and thus was illegal.

The second pertinent excerpt reads as follows:

> In *D'Oench,* the Supreme Court made clear the invalidity of defenses arising from defendants' *complicity* in a secret, irregular arrangement, even if the defendants' actions did not amount to fraud or illegality. *Id.* at 1171-1172 (emphasis added).

FDIC v. Hatmaker, 756 F.2d 34 (6th Cir. 1985).

Here is another case in which the borrower was attempting to avoid an obligation. The case was decided pursuant to 12 U.S.C. Sec. 1823(e), but is useful in interpreting the *D'Oench* doctrine.

In rejecting a defense based on a side agreement, the court said, "That such an agreement might have been fraudulently induced is immaterial; what is important is that the borrower *voluntarily* entered into such an agreement." *Id.* at 37 (emphasis added).

FDIC v. Castle, 781 F.2d 1101 (5th Cir. 1986).

This case is similar to *Hatmaker* in that the defendant was attempting to avoid liability on a note and the ruling was based on Sec. 1823(e). However, this case is also relevant to the *D'Oench* doctrine. The court relied on *Hatmaker* in ruling that fraudulent inducement of an agreement is irrelevant if the agreement was entered into voluntarily. *Id.* at 1107.

FDIC v. LeFeve, 676 F. Supp. 764 (S.D. Miss. 1987).

The defendant tried to avoid paying an amount owed to FDIC under a deed of trust. The court rejected the defendant's defenses, holding that "fraud by the lending institution does not alter the fact of *knowing participation* in the misleading arrangement," *Id.* at 769 (emphasis added), and "nor does lack of intent to defraud on the part of the debtor a[l]ter the fact of the debtor's *participation....*" *Id.* (emphasis added).

The court also cited with approval the above cited portions of *Hatmaker* and *Castle. Id.*

FDIC v. Investors Associates X., Ltd., 775 F.2d 152 (6th Cir. 1985).

The defendants were trying to avoid liability on two promissory notes. They signed blank notes based on a promise that the notes would not be enforced. This promise, or agreement, was the basis of their defense, and was found to be an arrangement likely to mislead the banking authorities. *Id.* at 155. The agreement sought to alter the plain terms of a facially sufficient document.

The court also held that *D'Oench,* at 315 U.S. 461, "explicitly stated that the maker would be liable even if 'ignorant of the fraudulent scheme, so long as he was *responsible* for the creation of the note.'" *Id.* at 154 (emphasis added).

FDIC v. Vestring, 620 F. Supp. 1271 (D.C. Kan. 1985).

FDIC sued on certain promissory notes. Defendants claimed no liability due to fraud in the inducement, estoppel, and failure of consideration. They also raised counterclaims based on the breach of an oral agreement with the bank and fraudulent misrepresentations by an agent of the

bank. The court rejected all defenses and counterclaims under *D'Oench,* saying that "it is clear that by entering into an oral agreement which contradicted the terms of the written note, the defendants did *lend* themselves to a deceptive secret agreement." *Id.* at 1273 (emphasis in original).

FDIC v. Cardinal Oil Well Servicing Co., Inc., 837 F.2d 1369 (5th Cir. 1988).

Fraud in the inducement was found to be no defense to the enforcement of certain guaranties because "the guarantors simply assert an oral side agreement not to enforce the guaranty agreements in accordance with their express terms." *Id.* at 1372.

Also, the guarantors could have revoked the guaranties at any time in writing. "By leaving unrevoked guaranties with the bank, the guarantors lent themselves to an arrangement which would tend to mislead the FDIC." *Id.*

FDIC v. McClanahan, 795 F.2d 512 (5th Cir. 1986).

McClanahan signed a blank promissory note, then delivered it to a man he knew had been convicted of bank fraud. When problems arose regarding this note, McClanahan only contacted this same man, who then forged McClanahan's signature on a renewal note. The court ruled that McClanahan's conduct was reckless, and thus his defenses of failure of consideration and fraud in the inducement were barred by *D'Oench. Id.* at 516-517.

Chatham Ventures, Inc. v. FDIC, 651 F.2d 355 (5th Cir. 1981).

The borrowers brought an action against FDIC challenging FDIC's right to collect on a note executed by borrowers. FDIC counterclaimed for enforcement of the note. The borrowers contended that the note was part of a joint venture

agreement with the lender under which the lender was to loan additional funds to borrowers. The lender never advanced these additional loans, and the borrowers argued that the lender thus breached the joint venture agreement, thereby relieving them of liability on the note. The alleged joint venture agreement, however, was only oral; therefore, it could not be asserted against FDIC. *Id.* at 362.

Please note that the borrowers were attempting to avoid liability on a specific asset, and had they prevailed on their claim a specific asset would have been adversely affected.

FSLIC v. Murray, 853 F.2d 1251 (5th Cir. 1988).

The defendants signed facially unqualified notes. As a defense to the notes, they asserted an agreement by the lender to fund additional loans and release them from liability upon sale of their shares of a partnership. Relying on *Langley, supra,* the court rejected this argument because it was based on an agreement which made facially unqualified notes subject to an unwritten and unrecorded condition. *Murray, supra,* at 1255.

Defendants also signed certain signature pages in blank. They claimed that these pages were later appended to documents other than those they intended to sign. This defense was rejected pursuant to *McClanahan, supra,* because such conduct was found to be reckless. *Murray, supra*.

Beighley v. FDIC, 868 F.2d 776 (5th Cir. 1989).

This case involved an affirmative claim by the borrowers based on the breach of an agreement by the lender to finance the purchase of certain property to a third party.

The decision is based on *Murray, supra*. The court made the following statements:

> We recently applied the *D'Oench, Duhme* doctrine to defeat an attempt by the makers of a note to

> *escape liability* by asserting that the lender violated an oral agreement to fund additional loans. *FSLIC v. Murray,* 853 F.2d 1251, 1255 (5th Cir. 1988). *Beighley, supra,* at 784 (emphasis added).

and

> Like the agreement in *Murray,* [the bank's] alleged oral agreement to finance future loans is not clearly evidenced in the bank's records, and would not be apparent to bank examiners. *Id.*

FDIC v. Huston, 1988 W.L. 97621 (N.D. Tex. 1988).

FDIC sought enforcement of guaranties against defendant Huston. Huston asserted as a defense an agreement that the guaranties were not to be enforced, and he claimed he signed the guaranties only because of that agreement. He also asserted a counterclaim based on the same agreement.

The key element in the decision is that Huston *voluntarily aqreed* to enter into the agreement and sign the guaranties. *Id.* at 6, 17 of slip opinion (attached). The court ruled that

> Thus if defendant Rex Huston was allowed to assert his side agreement as a basis for his counterclaim....he would be "relying on his *own wrongful act* to defeat the obligation of the note as against the receiver of the bank." *Id.* at 15, quoting *D'Oench* (emphasis added).

The court also stated that if Huston proved his counterclaim, the "FDIC's recovery on the *notes and guaranties* would be substantially less." *Id.* at 16 (emphasis added). In other words, the court linked recovery on the counterclaim to an adverse effect on a specific asset.

III. *AGREEMENT IS IN WRITING; THEREFORE IT IS NOT BARRED BY D'OENCH.*

It is a fact that the agreement was in writing in the form of a letter from Jobe, the Bank president. As a result, the

Bank did have a written record of the agreement, and Petitioners argue that such fact takes the agreement out from under *D'Oench*.

IV. *D'OENCH IS LIMITED TO AGREEMENTS ADVERSELY AFFECTING SPECIFIC ASSETS.*

On page 753 of its opinion, under headnotes 3 and 4, the Fifth Circuit analyzes — and dismisses — Petitioners' primary argument in both the trial and appellate courts. The opinion correctly summarizes the argument by saying that "the *D'Oench, Duhme* rule bars only claims or defenses based upon unrecorded side agreements that defeat the FDIC's interest in a *specific asset* acquired from a bank." *Bell & Murphy v. Interfirst Bank Gateway, N.A.*, 894 F.2d 750, 753 (5th Cir. 1990) (emphasis in original).

The *sole* authority on which the Fifth Circuit dismissed this argument was *Beighley, supra*. Petitioners will show that Beighley was an incorrect decision and/or an unjustified extension of the *D'Oench* doctrine.

Several aspects of *Beighley* serve as the foundation for the analysis below. The Beighleys instituted the litigation by suing the lender for breach of an agreement to finance a third party purchase of certain property. The FDIC eventually counterclaimed to enforce a note held by the FDIC. The appellate court held that the Beighleys' affirmative claims based on the agreement were barred by *D'Oench*.

Beighley is not supported by precedent. The actual application of the *D'Oench* doctrine in the *Beighley* opinion appears in two paragraphs on page 754. In those two paragraphs, three cases are cited, and only one of those addresses any of the relevant facts.

That one case is *Murray, supra*. The two cases are similar only in that they both involve agreements to finance some

sort of future loans. There is, however, a controlling difference. The borrowers in *Murray* were asserting a side agreement in order to *avoid liability* on a note held by the FDIC. As a result, the agreement necessarily would have adversely affected a *specific asset* held by the FDIC. In their suit, the Beighleys were not asserting a side agreement in order to avoid liability on a note. The Court will note that the agreement did eventually become the basis for defending liability on the note, but only *after* the FDIC filed a counterclaim for enforcement of the note. Petitioners argue that this fact alone renders *Murray* inapplicable to *Beighley* because the agreement in *Beighley* did not and could not relate to a specific asset. Therefore, *Beighley* is incorrect and cannot serve as authority for the judgment before this Court for review.

A closer look at *Murray* clearly shows that it is inapplicable to *Beighley*. The *Murray* court's specific ruling on the agreement to fund additional loans, *Murray, supra* at 1255, appears to be based on *Langley, supra,* thereby making it totally inapplicable to *Beighley* (in turn causing *Beighley* to be inapplicable to the case at bar). The agreement in *Langley* sought to alter the written terms of an unqualified note. The agreement in *Beighley* did not change the terms of the Beighleys' obligation. As stated, the Beighleys brought a suit for damages based on the breach of the agreement. They did not assert the agreement as an attempt to change or avoid the note until the counterclaim was filed, and those defenses were held barred by statute, not *D'Oench*. Also, the defenses necessarily related to a specific asset. The affirmative claim did not relate to a specific asset (if it did relate to a specific asset, then the appellate court's ruling in this case is clearly unsupported by precedent, for reasons which will be clearly explained in the conclusion of this argument). Consequently, any argument that *D'Oench* was applied to the

affirmative claim because the Beighleys were trying to avoid liabilty is meritless. It follows that the Beighleys' affirmative claims based on the agreement did not seek to change or alter their obligation on the note. Therefore, *Langley*, and hence *Murray*, is inapplicable to the facts of *Beighley*.

If the *Murray* court's ruling on the agreement to fund loans is not based on *Langley*, then it can only be based on *D'Oench*. After quoting a passage from *Langley*, the *Murray* court states

> Alliance's alleged oral agreements to fund additional loans and to release the Hintons from liability are simply secret side agreements that the Court invalidated almost fifty years ago in *D'Oench*, 315 U.S. at 460, 62 S. Ct. at 680. *Id.* at 1255.

There are several things to say in regard to the above passage. First, *D'Oench* alone does not support the Fifth Circuit's ruling in the case at bar. *D'Oench*, by its own terms, is limited to agreements which adversely affect specific assets. It is well established that the agreement in *D'Oench* concerned a specific asset, namely a note. Furthermore, it is without question that the agreement would have defeated the FDIC's interest in that specific asset. Therefore, the specific holding in *D'Oench* does not support any argument that the *D'Oench* doctrine is not limited to agreements which adversely affect a specific asset. The conclusion to be reached is as follows: 1) if the ruling in *Murray* regarding the agreement to fund future loans is based solely on *D'Oench*, then the ruling in *Beighley* is also based solely on *D'Oench*; 2) *D'Oench* alone does not support a ruling that the doctrine is not limited to the effect on specific assets; and 3) the ruling in *Beighley* is unsupported by precedent because the agreement there could not be shown to adversely affect a specific asset.

The bottom line is that the agreement to fund additional loans in *Murray* was barred because it either 1) was an unwritten agreement which sought to change the written terms of the note being sued upon, or 2) would otherwise have an adverse effect on a specific asset — the note being sued upon. The agreement to fund future loans in *Beighley* did not, and could not, have either of these effects. Consequently, the *Beighley* court's reliance on *Murray* is misplaced. This fact in turn means that there is no precedent supporting the ruling in *Beighley*. Stated differently, *Murray* is inapplicable to *Beighley*, and *Beighley* is in turn inapplicable to the case at bar.

The preceding analysis shows that *Beighley* does not support the Fifth Circuit's ruling that *D'Oench* is not limited to agreements that defeat the FDIC's interest in a specific asset. Such a result is very significant not only because *Beighley* is the sole authority cited for such ruling, but also because there are no other cases which support the ruling. With the exception of *Beighley*, all the cases discussed in the previous section of this petition involved agreements which would *adversely* affect the FDIC's interest in a *specific asset*. Petitioners do not know of any case other than *Beighley* in which *D'Oench* barred an agreement that did not adversely affect a specific asset.

Petitioners argue primarily that the judgment in question is not supported by precedent in any way, and should therefore be reversed. However, Petitioners argue further that there is no legal basis for the formation of a rule that *D'Oench* is not limited to agreements adversely affecting specific assets. The foundation of this argument is the language of 12 U.S.C. Sec. 1823(e). Even though the statute is technically inapplicable (since the FDIC is acting only as receiver and not in its corporate capacity), it is helpful in

determining the scope of the *D'Oench* rule. It has been held consistently that Sec. 1823(e) is a codification of the *D'Oench* doctrine. *Murray, supra* at 1254; *Taylor Trust v. Security Trust Federal Savings & Loan*, 844 F.2d 337, 342 (6th Cir. 1988). Furthermore, the *D'Oench* doctrine "has been extended considerably by the courts in interpreting the plain meaning of 12 U.S.C. Sec. 1823(e)," *In re the Matter of CTS Truss, Inc.*, 859 F.2d 357, 362 (5th Cir. 1988), and *D'Oench* has been used to interpret and apply the statute. Langley, *supra* at 401-402. With these considerations in mind, Petitioners will proceed with the argument.

The effect of the statute is limited to agreements concerning specific assets. The statute begins by saying, "No agreement which tends to diminish or defeat the right, title or interest of the Corporation in *any asset* acquired by it...." 12 U.S.C. Sec. 1823(e) (emphasis added). Given the emphasized language, the statute seems to indeed support the Fifth Circuit's ruling that *D'Oench* is not limited to specific assets, but another portion of the statute indicates otherwise. Section 1823(e) goes on to say that for an agreement to be valid, it must be in writing, and "(2) shall have been executed by the bank and the person or persons claiming an adverse interest thereunder, including the obligor, *contemporaneously with the acquisition of the asset by the bank. Id.* (emphasis added). Clearly, the first quote from the statute establishes that it applies to any assets acquired from a bank by the FDIC. However, the emphasized language in the second quote indicates that the statute applies to agreements related to *specific assets*. Why else would the statute say "with the acquisition of *the* asset?"

One may evaluate this argument by examining the results if it is incorrect. Assume that Sec. 1823(e) is not limited to

agreements adversely affecting specific assets. Also assume the following scenario:

1. Bank and Customer reach an agreement.
2. The agreement is that if Customer will immediately undertake an expansion of his business, Bank will provide him with loans to pay the cost of such expansion.
3. The agreement is in writing.
4. The agreement is executed by Customer and the Bank.
5. The agreement was approved by the Bank's board of directors, and such approval is noted in the board's minutes.
6. As soon as it was executed, the agreement was made an official record of the Bank.
7. Customer has no financial obligations owing to the Bank.
8. Customer immediately undertakes expansion of his business by buying additional supplies and inventory and hiring additional employees.
9. Once Customer takes these actions in reliance on the agreement, Bank then informs Customer that it will not provide him any loans.
10. Customer sues for damages caused by the Bank's breach of the agreement.
11. Shortly after the suit is filed, Bank fails and the FDIC acquires its assets through a purchase and assumption transaction.

Under the above scenario, will Customer's cause of action be barred by Sec. 1823(e)? It would seem that the suit would

not be barred. After all, the agreement was in writing, was approved by the Bank's board of directors, and was an official bank record. However, the agreement would be invalid under the statute, and hence the suit would be barred.

The statute plainly says that in order for an agreement to be valid, it must be executed "contemporaneously with the *acquisition* of *the* asset." *Id.* (emphasis added). The Bank did not acquire any asset as a result of the agreement. Furthermore, Customer had no previous loans or obligations with Bank, meaning that the Bank, and hence the FDIC, held no asset which had any connection to the agreement. As a result, Customer could not show that the agreement was executed contemporaneously with the acquisition of an asset.

This fact alone would not bar Customer's suit. The final blow would come from the fact that the agreement was the basis of a claim which could reduce the value of any given asset held by the FDIC. If the suit was allowed, and Customer prevailed, the FDIC would have to pay damages. Such action would reduce the total value of the assets held by the FDIC. Therefore, the agreement could adversely affect *any* asset held by the FDIC, and would be barred.

Suppose that Customer could prove that the agreement was executed contemporaneously with the acquisition of a specific asset. Seemingly, then, the agreement would be valid even though the suit could diminish the value of that asset, for all the requirements of the statute would be satisfied. The FDIC could simply claim that the agreement would not affect that asset but some other asset which was acquired by the Bank well before or after the execution of the agreement. As a result, Customer could not show that the agreement was executed contemporaneously with the acquisition of *the* asset affected by the agreement, meaning

that he could not satisfy the statute, and his suit would be barred.

In other words, in order to prosecute his claim, Customer would have to show that the agreement was executed contemporaneously with the acquisition of *every* asset held by the FDIC. Such a showing would, of couse, be impossible.

The above example shows what can happen if the statute is not limited to agreements which are related to and adversely affect a specific asset. Even if the agreement was in writing, was approved, and was an official record of the bank, the statute can be manipulated to bar the agreement.

If the statute could be manipulated as set out above, so too could the common law. The end result would be that any claim or defense ever raised against the FDIC would be barred (with the possible exception of those based on fraud in the factum as explained in *Langley, supra* at 402).

To further illustrate this point, assume an agreement which does involve a specific asset. Also assume that the agreement solidifies and/or enhances the bank's (and hence the FDIC's) interest in the asset. Under the Fifth Circuit's analysis, any defense or claim based in any way on such agreement would be barred because the litigation could adversely affect *any* asset held by the FDIC. It would not matter if the agreement was in writing and properly approved, executed, and recorded. The fact that the value of the specific asset involved would be enhanced would also be irrelevant.

Such a result is not only harsh and unjust to the "Customer," it does not fulfill any of the policies and objectives of the statute — or *D'Oench*.

The Fifth Circuit's ruling that *D'Oench* is not limited to agreements adversely affecting specific assets greatly

expands *D'Oench* — so much so that even written agreements and agreements which do not diminish the interest of the FDIC in an asset covered by the agreement could be barred. Such expansion of the law is not supported by precedent or principle.

CONCLUSION

The bottom line is that *D'Oench* is limited to agreements adversely affecting specific assets. This conclusion is of utmost importance to this case. The only specific asset of the Bank which was affected by the agreement was Petitioners' outstanding debt to the Bank. The agreement did *not* adversely affect that asset. In fact, the agreement *enhanced* the asset, for it placed in the Bank's control money over which it originally had no control or right, and, furthermore, a significant amount of this money was to be applied to the debt. The agreement ensured that payments would be made on the debt. Given these facts, there is no way the Bank's interest in its asset was diminished. Petitioners argue that since the Bank's interest was not adversely affected, the FDIC's interest in the asset was not adversely affected. Therefore, *D'Oench* is inapplicable.

There is an even more compelling reason why *D'Oench* is inapplicable. The one asset of the Bank affected by the agreement was never acquired by the FDIC. It is a fact that the Bank used all the funds obtained through the agreement to reduce Petitioners' indebtedness as quickly as possible. The FDIC has never once claimed that Petitioners owe any money. One would think that if Petitioners did owe money, the FDIC would have said so. In fact, the FDIC would have a *duty* to say so. This duty would be twofold: 1) in order to fulfill its legal mandate as receiver, the FDIC would be obligated to collect the money owed, and 2) the claim against Petitioners would be a *compulsory* counterclaim under Fed.

R. Civ. P. 13 (a). However, the FDIC has made no such claim. It can be inferred that Petitioners do not owe any money, meaning that there is no asset held by the FDIC which could be linked to the agreement, meaning further that the agreement did not and cannot adversely affect any specific asset acquired from the Bank by the FDIC. Consequently, *D'Oench* is not applicable.

V. *D'OENCH REQUIRES A SHOWING OF FAULT.*

Petitioners' secondary argument in the court below was that *D'Oench* required a showing of some sort of fault. This argument was supported in general by two cases. *Gunter v. Hutcheson,* 674 F.2d 862, 872 (11th Cir. 1982), cert. denied, 103 S. Ct. 60 (1982), stated that *D'Oench* required a showing of fault. Likewise, *FDIC v. Meo,* 505 F.2d 790, 793 (9th Cir. 1974), held that the defendant was "wholly innocent of any wrongdoing or negligence," and therefore *D'Oench* did not bar his defenses.

The Fifth Circuit totally dismissed the argument, and the analysis appears in three paragraphs under headnote 5 at 868 F.2d 753-754.

Before exposing the inherent weaknesses of the lower court's reasoning, Petitioners will establish the foundation of their position. The test for application of *D'Oench* is whether the borrower *lent himself* to a scheme or arrangement likely to mislead the banking authorities. *D'Oench, supra* at 460; *McClanahan, supra* at 715; *Investors Associates X, supra* at 154; *Vestring, supra* at 1273. If an obligor is totally innocent of fault, how has he *lent himself* to a scheme or arrangement? With this paramount question in mind, Petitioners will proceed with their argument.

Petitioners submit that there are several types of fault, all of which are presented below.

Voluntary participation

The following cases establish voluntary participation in a deceptive scheme or arrangement as a type of fault: *Castle, supra* at 1107; *Hatmaker, supra* at 37; *Huston, supra* at 6, 17; *LaFeve, supra* at 769.

Negligence or reckless conduct

McClenahan, supra, provides a prime example of this type of fault. Other examples are *Murray, supra,* and *Powers, supra,* in which the obligors signed documents in blank. *Cardinal Oil, supra,* shows another type of negligence in that the guarantors could have revoked the guaranties at any time but did not do so.

Knowingly contributing to a deceptive scheme

D'Oench gives rise to this type of fault. The obligor knew that the note in question was fraudulent, knew it was being used for a fraudulent purpose, and knowingly renewed the note. *D'Oench, supra* at 454, 459-460. Knowing contribution was also relied upon in *FDIC v. Leach,* 772 F.2d 1262, 1267 (6th Cir. 1985), and *FDIC v. Julius Richman, Inc.,* 80 F.R.D. 114, 117 (E.D.N.Y. 1978).

None of the above types of fault are present in the case at bar. Petitioners' suit is not based on agreements in which Petitioners volutarily took part. The suit is based on the breach of the agreement which went into effect on or about April 1, 1986. Given *Jenkins v. McKeithen, supra,* it is fact that Petitioners were fraudulently induced into taking action, and then the Petitioners were *forced* into accepting the "agreement" *under duress*. None of the types of negligent or reckless behavior discussed above occurred here. The only possible negligence committed by Petitioners could be their failure to discover that the Bank and Jobe were

making fraudulent misrepresentations and had no intention of honoring any agreement. Given Petitioners' previously good seventeen year history with the Bank, it is difficult to find fault with Petitioners in this respect.

The third type of fault is likewise absent. As shown, the agreement in question involved only one asset of the Bank, and that asset was not adversely affected. Therefore, the agreement made no misrepresentations about an asset of the Bank. Also, even if the previous sentence is incorrect, there is no indication that Petitioners knowingly had anything to do with such misrepresentation.

In short, Petitioners argue that 1) a showing of fault is required, 2) case law establishes three types of fault, and 3) none of the types of fault are present. The Fifth Circuit, however, rejected these contentions.

In so doing, the appellate court stated that it is irrelevant that Petitioners were coerced under economic duress to accept the agreement. *Bell & Murphy, supra,* at 754. This conclusion was based on three premises. The court stated in the first that in *D'Oench*,

> the Court there suggested that even a borrower who was "very ignorant and ill-informed of the transaction" and did not "intend to deceive any person" would likewise be precluded from asserting defenses based upon unrecorded side agreements that altered the terms of a facially unqualified note. *Id.* at 753 (quoting *D'Oench*).

Petitioners point out that the case at bar has nothing to do with altering the terms of a facially unqualified note — or any other asset of the Bank. The "very ignorant and ill-informed" language actually came from *Rinaldi v. Young,* 92 F.2d 229, 231 (D.C. Cir. 1937). That case also dealt with altering the terms of an obligation (and avoiding the obliga-

tion), and is likewise inapplicable to the case at bar. The issue of intent will be addressed later.

The appellate court used the inapplicable first premise as a step to the second premise, which states

> Moreover, numerous subsequent decisions have applied the *D'Oench, Duhme* rule in cases where the borrower was innocent of any wrongdoing, holding that the relevant question is not whether the secret agreement was itself fraudulent or whether the borrower intended to deceive banking authorities, but rather whether the borrower "lent himself to a scheme or arrangement" whereby those authorities were likely to be misled. *Id.* at 753-754 (citing *Beighley, supra*).

Petitioners again raise the question "if a borrower is completely innocent of any wrongdoing, how has he lent himself to a deceptive scheme?

The final premise says

> The *D'Oench, Duhme* doctrine thus favors the interests of depositors and creditors of a failed bank, who cannot protect themselves from secret agreements, over the interests of borrowers, who can. *Id.* at 754 (citing *Langley, supra,* and *McClanahan, supra*).

Petitioners do not disagree with the above statement; however, its application as a premise to the Fifth Circuit's conclusion on coercion is dangerous. If a borrower has been coerced into an agreement, how can he protect himself? The appellate court seems to think that he could and should "insist[] that the bank properly record the agreement." *Id.* A person who has been coerced is in no position to *insist* on anything, particularly a specific course of action by the coercing party.

Petitoners argue that if the basis for the ruling is unsound, the ruling itself is unsound. In any event, a close examination of the ruling itself shows its weakness. The ruling that coercion is irrelevant is in conflict with *FDIC v. Linn*, 671 F. Supp. 547 (E.D. Ill. 1987), which held that Sec. 1823(e) did not bar proof that a particular note did not reflect a valid agreement because the note was executed under economic duress. Given the relation between the statute and the common law, how can the defense of economic duress be allowed under one and not the other? Furthermore, examine this issue from a common sense point of view. If one is forced into an agreement, how did that person *lend* himself to the agreement? Petitioners urge that the answer is "he did not lend himself to the arrangement." In short, Petitioners argue that the appellate court's ruling on coercion and duress is ill-founded, in conflict with other precedent, and unsupported by precedent.

Now that Petitioners have critically analyzed the lower court's opinion, they must state that the opinion is correct on the issue of intent. However, such concession does not alter the fault argument, for it does not mean that a showing of fault is unnecessary. Intent has nothing to do with negligence, nor does it alter the fact that a person could intend not to deceive but nonetheless voluntarily enter into a precluded agreement. In other words, intent is not relevant in determining fault. The same reasoning applies to a person's knowledge (or lack thereof).

None of the authorities discussed herein say that *D'Oench* does not require a showing of fault. At most they say that such fault does not have to rise to the level of blatant illegality (such as intending to deceive or knowing an arrangement is fraudulent or deceptive).

Petitioners are unaware of any authorities stating that a showing of fault is not required. *Powers, supra,* does say that "*D'Oench* has been applied to bar defenses apparently not attributable to the conduct of the Defendants." *Id.* at 1171, citing only *Gunter, supra*.

A close examination of *Gunter* shows that the above statement from Powers is incorrect. *Gunter* was in no way based on *D'Oench*. There was no oral side agreement involved; hence, Sec. 1823(e) was inapplicable. *Id.* at 867. Since Sec. 1823(e) is a codification of *D'Oench*, it follows that *D'Oench* was also inapplicable. *Gunter* was decided on the basis of federal common law, but it was law newly created pursuant to *United States v. Kimbell Foods, Inc.,* 440 U.S. 715 (1979). *Gunter, supra* at 868-873. *Gunter,* therefore, does not support the above statement from *Powers.*

CONCLUSION

In conclusion, Petitioners argue that *D'Oench* requires a showing of fault, and the Fifth Circuit's reasoning and conclusions on the issue are incorrect. This conclusion is very significant, for Petitioners did not commit any fault, meaning that *D'Oench* is inapplicable.

VI. *THE ISSUE OF FRAUD IN THE INDUCEMENT*

The appellate court did not address the issue of fraudulent inducement, but Petitioners feel compelled to do so. Many cases hold that fraud in the inducement does not take an agreement out of the purview of *D'Oench* or Sec. 1823(e). Eight of the cases summarized earlier made such rulings. In four of those cases, the agreements sought to alter the written terms of an obligation. *Langley, supra; Investors Associates X, supra; Cardinal Oil, supra; Vestring, supra.* The other four cases involved agreements that were voluntarily entered into. *Castle, supra; Hatmaker, supra; Huston, supra;*

LaFeve, supra. All of the cases, then, contained allegations of fraud in the inducement *plus* some other factor. Neither of those factors are present in the case at bar. There has been no attempt to alter the terms of any obligation, and Petitioners did not voluntarily enter into the agreement. Therefore, Petitioners argue that their claims should not be dismissed only on the basis that they include allegations of fraudulent misrepresentation.

VII. *AGREEMENT NOT BARRED DUE TO BILATERAL OBLIGATIONS.*

The agreement in question established bilateral obligations between Petitioners and the Bank; therefore, the agreement is not barred. *Howell v. Continental Credit Corp.*, 655 F.2d 743, 746 (7th Cir. 1981). The appellate court dismissed this argument because the "alleged bilateral agreement...is unrecorded." *Bell & Murphy, supra,* at 754. There has been no evidence presented which shows directly or indirectly that the agreement was not recorded. On the other hand, it must be accepted as fact that the agreement was in writing and was written by the Bank president, Jobe. These facts indicate that the agreement was recorded. They certainly do not support the "finding" that the agreement was not recorded. Therefore, since the agreement was in writing and did establish bilateral obligations, *Howell, supra,* is applicable to this case.

PRAYER

Based on the preceding argument, Petitioners pray that this Court grant this Petition for Writ of Certiorari and resolve the issues presented herein. Petitioners further pray that this Court reverse the judgment of the Fifth Circuit Court of Appeals.

Respectfully submitted,

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BELL & MURPHY AND ASSOCIATES, INC., John W. Bell, Jr., Harold D. Barnett, Robert D. Hamer, Jr., and Richard L. Mears, ***Plaintiffs-Appellants,***

v.

INTERFIRST BANK GATEWAY, N.A., and Charles E. Jobe, ***Defendants-Appellees.***

No. 89-1719
Summary Calendar.

Unites States Court of Appeals, Fifth Circuit

Feb. 21, 1990.

Bank's customer brought action against bank based upon letter agreement pursuant to which bank was to extend open credit loans and honor certain checking account overdrafts in exchange for customer's surrender of its accounts receivable and funds from its pension and profit sharing plan to bank. The Federal Deposit Insurance Corporation (FDIC), intervening as receiver for insolvent bank, removed case to federal court. The United States District Court for the Northern District of Texas, at Fort Worth, Eldon B. Mahon, J., dismissed claims as barred by doctrine of *D'Oench, Duhme,* and appeal was taken. The Court of Appeals, Jerry E. Smith, Circuit Judge, held that: (1) unrecorded letter agreement was not enforceable against FDIC, and (2) *D'Oench, Duhme* rule applied to "bridge bank" authorized by FDIC to acquire assets and liabilities of failed bank.

Affirmed.

1. Federal Courts — 797

When reviewing dismissal of claim for failure to state claim, Court of Appeals, like district court, must accept material allegations of complaint as true and construe them

in light most favorable to nonmoving party. Fed.Rules Civ.Proc.Rule 12(b)(6), 28 U.S.C.A.

2. Banks and Banking — 505

Although Federal Deposit Insurance Corporation (FDIC) when acting in its receiver capacity cannot rely upon statutory protection given FDIC in its corporate capacity, FDIC in its receiver capacity is entitled to protection of common law *D'Oench, Duhme* rule which estops borrower from asserting against FDIC defense based upon secret or unrecorded side agreements that alter terms of facially unqualified obligations. Federal Deposit Insurance Act, § 2[13](e), 12 U.S.C.A. § 1823(e).

3. Banks and Banking — 505

D'Oench, Duhme rule, which precludes borrower from asserting against Federal Deposit Insurance Corporation (FDIC) defenses that are based upon secret or unrecorded side agreements that alter terms of facially unqualified obligations, bars not only claims or defenses based upon agreements that defeat FDIC's interests in specific asset acquired by bank, but also, affirmative claims based upon unrecorded agreements to extend future loans.

4. Banks and Banking — 505

Agreement under which customer was to surrender its accounts receivable and funds from its pension and profit sharing plans to bank, in return for which bank was to extend open corporate loans and to honor certain checking account overdrafts, thereby enabling customer to stay in business, was unenforceable under *D'Oench, Duhme* doctrine against Federal Deposit Insurance Corporation (FDIC) acting in its receiver capacity, where agreement was embodied in letter which was not contained in bank's records.

5. Banks and Banking — 505

D'Oench, Duhme doctrine which prohibits enforcement of side agreements against Federal Deposit Insurance Corporation (FDIC) applies not only to claims or defenses

based upon illegal side agreements entered into for purposes of deceiving bank authorities, but also to borrowers who are innocent of any wrongdoing.

6. Banks and Banking — 505

Exception to *D'Oench, Duhme* doctrine, for bilateral agreements made by failed banks was inapplicable to letter agreement entered into by bank's customer and bank, where alleged bilateral agreement which customer sought to enforce against Federal Deposit Insurance Corporation (FDIC) in its receiver capacity was unrecorded.

7. Banks and Banking — 505

D'Oench, Duhme rule, which precludes asserting against Federal Deposit Insurance Corporation (FDIC) defenses based upon secret or unrecorded side agreements that alter terms of facially unqualified obligations, extends to bridge bank authorized by FDIC to acquire assets and liabilities of failed bank.

Joseph E. Ashmore, Jr., Gregory Shamoun, Vassallo & Ashmore, Dallas, Tex., for plaintiffs-appellants.

Bruce L. Collins, William Frank Carroll, John Mitchell Nevins, Baker, Mills & Last, Dallas, Tex., for defendants-appellees.

Appeal from the United States District Court for the Northern District of Texas.

Before WILLIAMS, SMITH and DUHE, Circuit Judges.

JERRY E. SMITH, Circuit Judge:

Bell & Murphy and Associates, Inc., and four of its employees (collectively, "Bell & Murphy") filed suit in Texas state court against First RepublicBank Dallas, N.A. ("Republic"), and Republic officer Charles E. Jobe, seeking monetary damages for alleged fraudulent misrepresentations by the bank. The Federal Deposit Insurance Corporation ("FDIC") intervened as receiver for the insolvent

Republic, removed the case to federal district court, and then successfully moved to dismiss Bell & Murphy's claims as barred by the doctrine of *D'Oench, Duhme & Co. v. FDIC,* 315 U.S. 447, 62 S.Ct. 676, 86 L.Ed 956 (1942). We affirm.

I.

[1] Like many companies in the oil and gas industry, Bell & Murphy fell upon hard times in 1985.[1] Severe "cash flow" difficulties prompted the company to seek assistance from Republic, its longtime bank, and to agree to an arrangement suggested by bank officer, Charles E. Jobe. Under the terms of that agreement, Bell & Murphy was to surrender its accounts receivable and funds from its pension and profit sharing plans to the bank; in return, the bank was to extend open corporate loans and to honor certain checking account overdrafts, thereby enabling Bell & Murphy to stay in business. This agreement was embodied in a letter from Jobe to Bell & Murphy, but it was not reflected in Republic's records.

In April 1988, Bell & Murphy filed suit against Republic[2] in Texas state court, alleging that the bank had induced it to enter the agreement through fraudulent misrepresentations and then had breached its obligations under the agreement. Republic was declared insolvent in July 1988, and the FDIC was appointed as receiver pursuant to 12 U.S.C. § 1821(c). NCNB Texas National Bank, N.A. ("NCNB"), was then named by the FDIC to act as the "bridge bank" to acquire a portion of the assets and liabilities of the failed Republic.[3]

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[1] We state the facts as alleged in Bell & Murphy's complaint. This is appropriate, because when reviewing a Fed.R.Civ.P. 12(b)(6) dismissal we, like the district court, must accept the material allegations of the complaint as true and construe them in the light most favorable to the non-moving party. *See, e.g., Reid v. Hughes,* 578 F.2d 634, 637 (5th Cir. 1978).

[2] Jobe also was named as a defendant, but Bell & Murphy does not appeal the judgment in his favor.

[3] *See* 12 U.S.C. § 1821(n), authorizing the FDIC's use of bridge banks to acquire the assets and liabilities and to continue the normal banking operations of insolvent banks.

The FDIC then intervened in this action and removed it to federal district court, basing jurisdiction upon 12 U.S.C. § 1819. After considering extensive briefing by both sides, the district court concluded that even if Bell & Murphy's allegations were true, its claims were barred as to the FDIC and NCNB by the *D'Oench, Duhme* doctrine. The court therefore granted the defendants' motion to dismiss.

II.

A.

We begin our review of the judgment below with a brief discussion of the history and purposes of the *D'Oench, Duhme* rule. In *D'Oench, Duhme,* the defendant executed a note in favor of a bank in order to deceive state regulators by falsely inflating the value of the bank's assets. The defendant and the bank had agreed that the note would no be called for payment, but, for obvious reasons, this agreement was not reflected in the bank's records. Some years later, the bank obtained a loan from the FDIC, which took a security interest in the defendant's note. When the bank failed and the FDIC sued to collect on the note, the defendant raised the side agreement and also asserted that the note was invalid because it had been given without consideration.

The Supreme Court examined the statutory scheme that created the FDIC and concluded that it evidenced a "federal policy to protect ... [the FDIC] and the public funds which it administers, against misrepresentations as to ... the assets in the portfolios of the banks which ... [the FDIC] insures or to which it makes loans." *D'Oench, Duhme,* 315 U.S. at 457, 62 S.Ct. at 679. In order to effect this federal policy, the Court fashioned a common law rule of estoppel precluding a borrower from asserting against the FDIC defenses based upon secret or unrecorded "side agreements" that altered the terms of facially unqualified obligations.

[2] Congress later ratified the result in *D'Oench, Duhme* by enacting 12 U.S.C. § 1823(e), which affords the FDIC,

when acting in its corporate capacity, comprehensive protection against any

> . . . agreement which tends to diminish or defeat . . . [its] interest . . . in any asset acquired by it . . . unless such agreement (1) is in writing, (2) was executed by the depository institution and . . . the obligor, contemporaneously with the acquisition of the asset by the depository institution, (3) was approved by the board of directors of the depository institution or its loan committee, which approval shall be reflected in the minutes of said board or committee, and (4) has been continuously, from the time of its execution, an official record of the depository institution.

Although the FDIC may not rely upon the enumerated requirements of section 1823(e) where, as here, it acts as receiver rather than in its corporate capacity, *see FDIC v. McClanahan,* 795 F.2d 512, 516 (5th Cir. 1986), it is nonetheless entitled to the protection of the common law *D'Oench, Duhme* rule. *See Beighley v. FDIC,* 868 F.2d 776, 783 (5th Cir. 1989). With this background in mind, we now examine each of Bell & Murphy's efforts to take its claims outside the scope of the *D'Oench, Duhme* doctrine.

B.

[3] Bell & Murphy first advances the argument that the *D'Oench, Duhme* rule bars only claims or defenses based upon unrecorded side agreements that defeat the FDIC's interest in a *specific asset* acquired from a bank. According to Bell & Murphy, the side agreement at issue here, while affecting Republic's total worth, does not diminish the value of Bell & Murphy's admitted outstanding debt to Republic. The side agreement thus could not have misled the FDIC regarding the value of Republic's assets, and *D'Oench, Duhme* does not preclude Bell & Murphy from asserting that side agreement against the FDIC.

[4] We find this inventive argument to be meritless in light of our recent holding in *Beighley* that the *D'Oench, Duhme* rule bars affirmative claims based upon unrecorded

agreements to extend future loans. There, we noted that the "alleged oral agreement to finance future loans . . . [was] not clearly evidenced in the bank's records, and would not . . . [have been] apparent to bank examiners." 868 F.2d at 784. Although the agreement that Bell & Murphy seeks to enforce against the FDIC allegedly is embodied in a letter, it was not contained in Republic's records. Thus, it could not have been discovered by bank examiners and is not enforceable against the FDIC.

[5] We can dispense easily with Bell & Murphy's contention that the *D'Oench, Duhme* rule bars only claims or defenses based upon *illegal* side agreements entered into for the purpose of deceiving banking authorities. Although the obligor in *D'Oench, Duhme* was in fact a knowing participant in such a fraudulent scheme, the Court there suggested that even a borrower who was "very ignorant and ill-informed of the transaction" and did not "intend[ ] to deceive any person" would likewise be precluded from asserting defenses based upon unrecorded side agreements that altered the terms of a facially unqualified note. *D'Oench, Duhme,* 315 U.S. at 458-59, 62 S.Ct. at 679-80.

Moreover, courts in numerous subsequent decisions have applied the *D'Oench, Duhme* rule in cases in which the borrower was innocent of any wrongdoing, holding that the relevant question is not whether the secret agreement was itself fraudulent or whether the borrower intended to deceive banking authorities, but rather whether the borrower "lent himself to a scheme or arrangement" whereby those authorities were likely to be misled. E.g., *Beighley,* 868 F.2d at 784 (quoting *D'Oench, Duhme,* 315 U.S. at 460, 62 S.Ct. at 681). The *D'Oench, Duhme* doctrine thus favors the interests of depositors and creditors of a failed bank, who cannot protect themselves from secret agreements, over the interests of borrowers, who can. *See Langley v. FDIC,* 484 U.S. 86, 94, 108 S.Ct. 396, 402, 98 L.Ed.2d 340 (1987); *McClanahan,* 795 F.2d at 916.

Hence, it is irrelevant to the applicability of the *D'Oench, Duhme* rule whether Bell & Murphy acted in good faith and

even whether Bell & Murphy was "coerced," under "economic duress," into accepting the terms of the agreement proposed by Republic. Bell & Murphy could have protected itself by insisting that the bank properly record the agreement; because it did not, it is estopped from asserting any claims arising out of the bank's alleged secret promise to make future loans.

[6] Relying heavily upon *Howell v. Continental Credit Corp.*, 655 F.2d 743 (7th Cir. 1981),[4] Bell & Murphy next contends that the *D'Oench, Duhme* doctrine does not bar its claims because they are based upon the breach of an agreement that imposes obligations upon *both* parties. While *Howell* indeed does contain somewhat expansive language to the effect that the FDIC is bound by bilateral agreements made by failed banks, a close reading of that decision reveals that the bilateral obligations at issue there appeared on the face of the written, properly recorded agreement which the FDIC sought to enforce.

In *Howell,* a bank promised to purchase certain equipment which it would then lease to Howell. The various leases, which were contained in the bank's records, clearly manifested the bank's obligation to obtain title to the equipment. When the FDIC sued Howell to collect payments due under the leases, Howell sought to defend on the ground that the bank in fact had never obtained title to the equipment and that she had never leased it. The court concluded that Howell should be allowed to present this defense, finding *D'Oench, Duhme* inapplicable where "the document the FDIC seeks to enforce is one, such as the leases here, which *facially manifests* bilateral obligations and serves as the basis of the leasee's defense." *Howell,* 655 F.2d at 746 (emphasis added). *See also FDIC v. O'Neil,* 809 F.2d 350, 354 (7th Cir. 1987) (noting that the dispositive fact in *Howell* was that "[t]he conditions that Mrs. Howell sought to enforce against the FDIC's asset ... appeared in the asset itself ...").

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[4] *Howell* was cited approvingly by this circuit in *McClanahan,* 795 F.2d at 515.

Here, the alleged bilateral agreement which Bell & Murphy seeks to enforce against the FDIC is unrecorded. Therefore, the narrow exception recognized in *Howell* does not take Bell & Murphy's claims outside the scope of *D'Oench, Duhme.*

[7] Finally, Bell & Murphy asserts that *D'Oench, Duhme* protections, even if applicable, do not bar a recovery against NCNB, the bridge bank authorized by the FDIC to acquire the assets and liabilities of the failed Republic. However, we agree with the FDIC that failure to extend *D'Oench, Duhme's* protection to bridge banks would undermine the effectiveness of bridge banks as a means of continuing the normal banking operations, and thereby protecting the depositors and creditors, of a failed bank. Moreover, our holding in *FSLIC v. Murray,* 853 F.2d 1251, 1256 (5th Cir. 1988), that the *D'Oench, Duhme* rule provides holder-in-due-course status to the FDIC compels the conclusion that assignees of the FDIC also enjoy protection from claims or defenses based upon unrecorded side agreements.[5] Accordingly, we hold that claims barred as to the FDIC by the *D'Oench, Duhme,* doctrine likewise are barred as to bridge banks authorized by the FDIC to take over the operations of a failed bank.

In sum, we agree with the district court that even if Bell & Murphy's allegations are true, they do not state a claim upon which relief can be granted against either the FDIC or NCNB. Accordingly, the judgment of the district court dismissing Bell & Murphy's claims pursuant to Rule 12(b)(6) is AFFIRMED.

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[5] *See also FDIC v. Newhart,* 713 F.Supp. 320, 324 (W.D.Mo.1989) (subsequent holder of note acquired from FDIC also acquires FDIC's holder-in-due-course status); *RSR Properties, Inc. v. FDIC,* 706 F.Supp. 524, 531 (W.D.Tex.1989) (claims barred as to FDIC are equally barred as to bridge bank NCNB because of FDIC's holder-in-due-course status).

U.S. COURT OF APPEALS
FILED
FEB 21, 1990
GILBERT F. GANUCHEAU,
CLERK

United States Court of Appeals
FOR THE FIFTH CIRCUIT

NO. 89-1719
Summary Calendar

D.C. Docket No. CA4-88-553-E

BELL & MURPHY AND ASSOCIATES, INC., ET AL.,
Plaintiffs-Appellants,
versus
INTERFIRST BANK GATEWAY, N.A. and
CHARLES E. JOBE,
Defendants-Appellees.

Appeal from the United States District Court for the Northern District of Texas

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Before WILLIAMS, SMITH and DUHE, Circuit Judges.

JUDGMENT

This cause came on to be heard on the record on appeal and was taken under submission on the briefs on file.

ON CONSIDERATION WHEREOF, It is now here ordered and adjudged by this Court that the judgment of the District Court in this cause is affirmed.

IT IS FURTHER ORDERED that plaintiffs-appellants pay to defendants-appellees the costs on appeal to be taxed by the Clerk of this Court.

February 21, 1990

ISSUED AS MANDATE: MAR 15 1990

FILED
TARRANT COUNTY, TEXAS
'88 APR 25 P3:42
THOMAS P. HUGHES
DISTRICT CLERK

NO. 352-112460

IN THE 352 JUDICIAL DISTRICT COURT OF TARRANT COUNTY, TEXAS

BELL & MURPHY AND ASSOCIATES, INC.,
JOHN W. BELL, JR., HAROLD D. BARNETT,
ROBERT D. HAMER, JR., and RICHARD L. MEARS
Plaintiffs,

vs

INTERFIRST BANK GATEWAY, N.A.
and CHARLES E. JOBE,
Defendants.

PLAINTIFF'S ORIGINAL PETITION

TO THE HONORABLE JUDGE OF SAID COURT:

COMES NOW, BELL & MURPHY and ASSOCIATES, INC., ("BMA") JOHN W. BELL, JR., HAROLD D. BARNETT, ROBERT D. HAMER, JR. and RICHARD L. MEARS, Plaintiffs, complain of Defendants, INTERFIRST BANK GATEWAY, N.A. ("INTERFIRST") and CHARLES E. JOBE and respectfully show the Court the following:

I.
PARTIES

1. Plaintiff Bell & Murphy and Associates, Inc. is a Texas Corporation, duly formed and existing under the laws of the State of Texas and has its principal place of business in Dallas, Dallas County, Texas.

2. Plaintiffs John W. Bell, Jr. and Robert W. Hamer, Jr. are residents of Dallas, Dallas County, Texas.

3. Plaintiff Harold D. Barnett is a resident of Denton, Denton County, Texas.

4. Plaintiff Richard L. Mears is a resident of Midland, Texas.

5. Defendant Interfirst Bank Gateway, N.A., is a corporation having its principal office in Tarrant County, Texas. Defendant Interfirst may be served with citation by delivery of citation to its president, Charles E. Jobe at 3532 Joyce, Fort Worth, Texas 76116.

6. Defendant Charles E. Jobe is an individual resident of Fort Worth, Tarrant County, Texas and may be served with process by mailing a true copy of the citation with a copy of Plaintiff's Petition attached thereto, by certified mail, delivery restricted to addressee only, return receipt requested, to Jobe's place of business located at Interfirst Bank Gateway, N.A., 3532 Joyce, Fort Worth, Texas 76116.

II.
JURISDICTION AND VENUE

7. Venue is proper in Tarrant County, Texas pursuant to Section 15.001, Texas Civil Practice and Remedies Code. This is an action for fraud with the subject matter of this action having occurred in Fort Worth, Tarrant County, Texas.

III.
BACKGROUND

8. All Plaintiffs have joined in this action due to the fact that the cause of action asserted herein arises out of a transaction common to all Plaintiffs. Consequently, this action can be said to involve the same questions of law and the same questions of fact with respect to each Plaintiff's claim against Defendants.

9. Plaintiffs in this action are comprised of former officers and former employees of BMA.

10. BMA's primary business objectives involved consultation, interpretation of seismic data and exploration for potential oil and gas reservoirs.

11. Due to the general nature of the Texas ecomony and the nature of the oil and gas industry as a whole, BMA's financial condition in 1985 was deteriorating. In 1985 BMA began experiencing cash flow problems as well.

12. As a result of a seventeen (17) year history at InterFirst, BMA established a quality reputation. As a result, BMA's cash flow problems were countered by Defendants in 1985.

13. In 1985, Defendants verbally agreed to honor all payroll tax checks that resulted in an overdraft on BMA's checking account.

14. By April of 1986, Defendants effectively controlled the corporate operations of BMA, and at this point Defendants arbitrarily honored certain checks while not honoring other checks issued by BMA.

15. Specifically, Defendants no longer honored checks written by BMA to the Internal Revenue Service expressly for payroll tax purposes. Defendants had knowledge that said checks were for payroll taxes as they were duly labeled and presented, by BMA, to Defendants. Defendant, in violation of the verbal agreement, did not cover BMA checks for payroll taxes in the second, third and fourth quarter of 1985 and the first quarter of 1986.

16. As a result of BMA's continuing financial problems, Defendants began demanding that BMA to obtain corporate loans from BMA's pension plan and profit sharing plan.

17. BMA, desiring to continue its relations with Defendant on the best possible level, attempted to obtain loans from its profit sharing plan and its pension plan. It was determined that BMA would have to follow a procedure, as per Employee Retirement Income Security Act, which would require a minimum of six to nine months before the loans could be obtained.

18. Defendants, at that time, were unwilling to wait six months and told BMA to find a way to get a loan from these plans. BMA determined that its employees could borrow from these plans on an individual basis whereupon each individual would loan these monies to BMA.

19. Defendants demanded BMA obtain these loans. In January 1986, Jobe wrote an offer stating "an investment from BMA was now required to keep it in operation". This offer was presented to the employees of BMA. The offer provided for the funds from the pension plan to be used to cancel a portion of the debt held by Defendants. The funds from the profit sharing plan were to be used to extinguish a debt held by the Internal Revenue Service.

20. The letter agreement by Defendants was a fraudulent inducement to the employees of BMA. The bank used the letter to fraudulently gain control of the assets beyond the bank's control.

21. Once this proposed offer was accepted by BMA and its employees and once the process of obtaining these loans was well on its way to completion, Defendant notified BMA that its original plan was not sufficient. At this point, Defendants demanded that the loans from each plan be lumped together whereupon a two-thirds share of all monies was to be taken by Defendant and one-third was to be given to the Internal Revenue Service. BMA, as a result of its economic position, had no viable alternatives when Defendant, contrary to its original offer which had been accepted by Plaintiffs, shifted its position. This shift in position by the bank caused Plaintiffs to accept Defendants offer under economic duress.

22. The Contract structured according to Jobe's whim fell into place on or about April 1, 1986. This Contract called for BMA's account receivables to be paid to Defendants, it called for the employees individual loans to the corporation to be paid two-thirds to the Defendant and one-third to the Internal Revenue Service; it called for BMA to change its pay period to semi-monthly; it called for BMA to reduce the salaries of its senior executives to a level that only met

minimum living obligations and the agreement called for BMA to reduce the pay to other employees and officers of BMA by fifteen percent.

23. All of the conditions imposed by Defendants upon BMA were met. The agreement, in effect, was designed to allow BMA to continue to operate while Defendants were to loan money to BMA for any overdrafts, including payroll checks, checks to the Internal Revenue Service for payment of withholding taxes and other checks for necessary operating expenses.

24. Defendants during the operation of the agreement were continually recovering monies from BMA's accounts receivables. At least one million dollars in consulting fees were being billed on an annual basis and at no time did the overdraft account exceed the total amount owed to BMA.

IV.
CAUSE OF ACTION

25. As a result of BMA's total compliance with every obligation of the letter agreement imposed by Defendants, BMA was to have been able to operate without limitation. In other words, Defendant was obligated to "work" with the corporation and was to extend open corporate loans so long as BMA complied with the terms of the agreement.

26. Defendants InterFirst and Jobe, upon extending the offer to BMA, knew that BMA was on the verge of financial ruin. Defendants also knew that it stood to lose money if BMA failed prior to obtaining loans from its profit sharing plan and pension plan.

27. As a result of this knowledge, Defendants knowingly made false representations of material facts to BMA. Said misrepresentations were made with the intent to induce Plaintiffs to obtain loans from their profit sharing and pension plans so that Defendant could reduce the outstanding balance owed by BMA.

28. Plaintiffs submit the above representations concerned material facts for the reason that Plaintiffs would not have pursued and obtained loans from either the profit sharing plan or the pension plan had Defendant's intent (to reduce the sum owed by BMA as quickly as possible without regard to whether BMA survived the economic crisis it was experiencing) been known by Plaintiffs. The above representations of Defendant were relied on by Plaintiffs to their substantial injury and damage.

V.
DAMAGES

29. By reason of Plaintiffs' reliance upon Defendants' misrepresentations described above, Plaintiffs have been damaged in an amount in excess of the minimum jurisdictional limits of the Courts.

30. Plaintiffs further allege that by reason of the fact that Defendants knew that the representations were false at the time they were made, said representations were willful and malicious and constitute conduct for which the law allows the imposition of exemplary damages. In this connection Plaintiffs will show that they have incurred significant expenses, including attorney's fees, in the investigation and prosecution of this action. Accordingly, Plaintiffs request that exemplary damages be awarded against the Defendant in a sum which exceeds the minimum jurisdictional limits of the Court.

WHEREFORE, PREMISES CONSIDERED, Plaintiff prays that Defendant be cited to appear and answer and that on final trial, Plaintiff have:

1. Judgment against Defendants for actual damages in a sum in excess of the minimum jurisdictional limits of the Court, with interest at the lawful rate from April 1, 1988 until Judgment;

2. Judgment against Defendants for exemplary damages in a sum to be determined by the trier of fact;

3. Interest after Judgment at the rate of 10 percent per annum until paid;

3. Costs of suit; and

5. Such other and further relief to which Plaintiff may be justly entitled.

Respectfully submitted,
VASSALLO & ASHMORE, P.C.

By: JOSEPH E. ASHMORE, JR.
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U.S. DISTRICT COURT
NORTHERN DISTRICT
OF TEXAS
FILED
AUG 22, 1988
NANCY DOHERTY, CLERK
By ________ CF________
Deputy

IN THE UNITED STATES DISTRICT COURT FOR THE NORTHERN DISTRICT OF TEXAS WICHITA FALLS DIVISION

CIVIL ACTION NO. CA 7-87-62

FEDERAL DEPOSIT INSURANCE CORPORATION,
as Receiver for
FIRST NATIONAL BANK OF OLNEY, OLNEY TEXAS
and in its Corporate Capacity,

versus

REX M. HUSTON.

ORDER

Before the Court is Plaintiff's Motion for Summary Judgment. Plaintiff, the Federal Deposit Insurance Corporation (FDIC), contends that it is entitled to judgment as a matter of law on the notes and guaranties it holds. Plaintiff contends that the notes are due and payable and Defendant's asserted defenses are invalid as a matter of law under section 1923(e) of Title 12, United States Code and the federal common law.

Defendant Rex Huston contends that Plaintiff is not entitled to judgment as a matter of law because his defenses and counterclaim are not precluded by section 1823(e) or the federal common law. Defendant has asserted the defenses of usury, fraudulent misrepresentation and lack of consideration. He has also counterclaimed against the FDIC in its receivership capacity and corporate capacity for usurious interest.

The following facts are undisputed for purposes of this motion for Summary Judgment:

1. In 1982, Defendant approached First National Bank of Olney (the Bank) for a loan. Mr. Conley, vice-president of the Bank informed him that he would not receive the loan unless he signed certain guaranties.

2. The guaranties were on loans to acquaintances of Defendant, Tommy Ballard, and Barbara Robinson, for a total sum of $59,250.00, which were due and owing at that time.

3. Mr. Conley represented to Defendant that the guaranties would never be used, they were only needed to satisfy the bank examiners.

4. Defendant signed three blank guaranties.

5. Subsequently Defendant received a loan in the amount of $110,000.00 with interest at the rate of 15.5%.

6. Later Defendant received two other loans, one in the amount of $20,000.00, the other for $70,000.00.

7. The Bank instituted suit against Defendant Huston for payment of the notes and guaranties in December, 1984.

8. Defendant responded asserting usury as a counterclaim and defense. Later he amended his pleadings to assert lack of consideration and fraud in the inducement as affirmative defenses.

9. On March 12, 1987 the Bank was declared insolvent.

10. The FDIC in its receivership capacity assumed control of the bank. It then sold all the Huston notes and guaranties to FDIC in its corporate capacity. However the FDIC in its receivership capacity kept the liabilities of the Bank, including the asserted counterclaim pending in the state court suit.

11. The FDIC then intervened in the state court suit and removed the case to federal court.

Upon these facts Plaintiff now moves this Court for Summary Judgment contending that it is entitled to Judgment as a matter of law.

Defendant alleges that he is not liable on the guaranties because the facts, above, establish lack of consideration. The guaranties were on loans that had already been made and which were past due when the guaranties were signed, thus there was no consideration for the signing of the guaranties. Further Defendant alleges that the signature on the guaranties were procured by fraud. Mr. Conley represented to Defendant that the guaranties would not be called in, and relying on such representation, Defendant did sign the guaranties.

Defendant also alleges that since the guaranties were signed as a prerequisite to the approval of his $110,000.00 loan then such amount due on the guaranties are in the nature of interest on that loan. Defendant contends that the interest on the face of the note and the amount of the guaranties together constitute usurious interest on the $110,000.00 note.

The parties have agreed to an analytical framework encompassing two distinct elements of the lawsuit. These are: (A) FDIC's claim for affirmative relief on the guaranties and notes brought in its corporate capacity and (B) Huston's claim for affirmative relief for usury damage brought against FDIC in its receivership and corporate capacities. Accordingly the Court will use this same framework to determine the issues before it.

A. FDIC'S CLAIMS ON THE NOTES AND GUARANTIES:

The FDIC seeks judgment on three notes and three guaranties signed by Defendant Huston. They are:

a. The note for $110,000.00 dated September 22, 1982.[1]

[1] Plaintiff in its supporting affidavit requests judgment on the entire $110,000.00. However Plaintiff's petition requested relief for $74,722.40 as the remaining unpaid balance on the note. The petition alleges that

b. The note for $70,468.92 dated November 10, 1982.

c. The note for $20,000.00 dated April 28, 1983.

d. Guaranty for a note signed by Tommy Ballard in the amount of $15,000.00 dated September 15, 1982.

e. Guaranty for a note signed by Barbara Robinson in the amount of $25,000.00 dated September 15, 1982.

f. Guaranty for a note signed by Barbara Robinson in the amount of $19,250.00 dated September 15, 1982.

Defendant contends that he is not liable on the $110,000.00 and the guaranties because of usury.[2] Further he alleges that he is not liable on the guaranties because of fraud in the inducement and lack of consideration. Plaintiff alleges that Defendant's defenses and counterclaim are based upon an oral side agreement that "tends to diminish its interest" in the notes and thus the agreement cannot be considered pursuant to 12 U.S.C. section 1823(e).

Section 1823(e) of Title 12, United States Code, states:

> No agreement which tends to diminish or defeat the right, title or interest of the Corporation in any asset acquired by it under this section, either as security for a loan or by purchase, shall be valid against the corporation unless such agreement (1) shall be in writing, (2) shall have been executed by the bank and person or persons claiming an adverse interest thereunder, including the obligor, contemporaneously with the acquisition of the asset by the bank, (3) shall have been approved by the board of directors or its loan committee, which approval shall be reflected in the minutes of said

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payment of $64,798.22 was made on the note, the sum of $35,277.50 was applied to the principle and the sum of $29,520.72 was applied to interest. No amended petition seeking the entire amount has been filed. Thus if the Court awards any relief it will be in the amount requested in the petition.

[2] Defendant admits his liability on the other two notes, and offers no defense to them. However Defendant intends to offset these notes by the usury damages he hopes to prove.

> board or committee, and (4) shall have been, continuously, from the time of its execution, an official record of the bank.

It is undisputed that the alleged arrangement between the bank and Defendant Rex Huston was oral and not part of the bank records. Further none of the documents referred to such an arrangement.

1. Fraud in the inducement:

Defendant argues that accepting the facts as alleged he was fraudulently induced to sign the notes because at the time he did sign the three blank guaranties the vice-president of the bank, Richard Conley, represented to him the guaranties would not be used, that they were protection for the bank and for the regulators. That the guaranties would stay in Mr. Conley's desk and Defendant would not be called on to perform on those guaranties. *See* Deposition of Rex Huston, at 38.

Plaintiff argues that this agreement between the Bank and Defendant is invalid because it clearly violated section 1823(e). The Court agrees.

The purpose of the statute is:

> to protect the FDIC from the hidden agreements that would defeat its interest in what is otherwise a facially valid note. Such hidden agreements would prevent the FDIC from accurately valuing assets and from making informed decisions on how best to handle a bank's insolvency. The concern is thus with agreements that are not made part of the note. *Federal Deposit Insurance Corporation v. Castle.* 781 F.2d 1101, 1107 (5th Cir. 1986) (citations omitted).

Thus "[t]hat such an agreement might have been fraudulently induced is immaterial; what is important is that the borrower voluntarily entered into such a *side* agreement." *Id.* at 1107. There has been no suggestion that the

Defendant did not voluntarily enter the agreement. The deposition testimony reveals that Defendant did sign the guaranties in question after the representation was made to him. *See supra.*

Thus the Court finds that Defendant's asserted defense of fraud in the inducement is invalid as against the FDIC since such defense depends on a side oral agreement that diminishes the interest of the FDIC in the guaranties.[3]

2. Lack of Consideration:

Defendant alleges that he is not liable on the guaranties because there was no consideration for his signature on those guaranties. He alleges that the underlying notes on which the guaranties were given were already due and payable, thus no value was given for the guaranty.

Under Texas law, a valuable consideration for a contract is either benefit to the promisor or detriment to the promisee or a surrender by the promisee of some legal right. *El Paso County Water Imp. Dist. No. 1 v. City of El Paso*, 243 F.2d 927 (5th Cir.) *cert. denied,* 355 U.S. 820 (1957). When two instruments are executed as part of the same transaction, the benefit accruing to one of the parties in one instrument may be consideration for promise of such party in the other. *Mitchell v. Lawson,* 444 S.W.2d 192 (Tex. Civ. App.—San Antonio 1969, no writ).

The acts as alleged by Defendant, and as accepted by Plaintiff for purposes of this motion, reveal that the Defendant did indeed receive consideration. Defendant testified that he signed the guaranties in return for the bank's

[3] The court notes that the FDIC has been allowed to recovery on very similar facts. *Federal Deposit Insurance Corporation v. Powers,* 576 F.Supp. 1167 (N.D. Ill. 1983), *aff'd.* 753 F.2d 1076 (7th Cir. 1984) (cited with approval in *Federal Deposit Insurance Corporation v. Castle.* 781 F.2d 1101, 1107 (5th Cir. 1986). In *Powers* the defendant signed a guaranty in blank but with the understanding that he was not guaranteeing the underlying obligation. The understanding was oral and not part of the loan record. There the Court held that under section 1823(e) the Defendant was estopped from asserting this understanding as a defense to the guaranty.

loan to him of $110,000.00. *See* Deposition of Rex Huston at 32. Thus Defendant has no defense for lack of consideration under his version of the facts.

3. Usury:

Defendant contends that he is not liable on the $110,000.00 and the guaranties because the FDIC is attempting to collect usurious interest. He contends that he signed the guaranties as a precondition to the $110,000.00 note and that under Texas law this rendered the guaranties a form of interest on that note in addition to the interest on the face of the note in the amount of 15.5%. Defendant asserts that the guaranties and the stated interest constitute more than a 100% rate of interest on the note and that such rate is usurious.

Further he maintains that the usury defense is not based upon "an 'agreement' which, in and of itself, tends to diminish the rights of the FDIC in the $110,000.00 note and Guaranties. Huston's defense to the $110,000.00 Note and the Guaranties does not depend upon an agreement that the Guaranties and notes not be enforced in accordance with their terms. Rather, Huston's defense arises by operation of the applicable usury statutes." *Defendant's Brief in Support of Response to Motions for Summary Judgment* at 9-10.

However before the usury statutes can be applied, Defendant must establish the arrangement he and the bank entered into. The application of the statute depends on the arrangement, without this arrangement there would be no usury. Thus the arrangement is being used to diminish the FDIC's interest in the note and guaranties.

For purpose of this Motion for Summary Judgment the FDIC has accepted Defendant's contentions on the guaranties and $110,000.00 note as true. Therefore assuming that the parties did enter into an arrangement whereby Defendant signed three blank guaranties and the Bank, in turn, loaned Defendant $110,000.00, the question as to whether this arrangement was an agreement remains.

The Supreme Court in *Langley v. Federal Deposit Insurance Corporation,* 108 S.Ct. 396. 401 (1987) held that "[a]s used in commercial and contract law, the term 'agreement' often has 'a wider meaning than... promise.'...(citations omitted)." Further the court held that the term "agreement" as used in section 1823(e) should be given the common meaning of such word. " 'Agreement' in section 1823(e) covers more than promises to perform acts in the future, it also covers conditions precedent to the maker's performance." *Id.* at 402. Thus such a condition "is part of the 'agreement' to which the writing, approval and filing requirements of 12 U.S.C. section 1823(e) attach." *Id.* at 403.

Therefore Defendant's own testimony that the signing of the guaranties was a "precondition" to the loan of $110,000.00 defeats his argument that such an arrangement was not an agreement.

Defendant argues that even if it was an agreement it was not the type of agreement contemplated by the statute. However "[t]he language of the statute is all encompassing; any agreement is subject to the statute if it tends to defeat or diminish FDIC's rights in an asset purchased under authority of section 1823." *Federal Deposit Insurance Corporation v. Hoover-Morris Enterprises,* 642 F.2d 785, 787 (5th Cir. 1981). Thus any defense which emanates from a party's secret agreement having the effect of misinforming the FDIC, is barred by the FDIC's statutory protections. *Federal Deposit Insurance Corporation v. Langley,* 792 F.2d 541, 546 (5th Cir. 1986). *aff'd.* 108 S.Ct. 396, (1987).

In *Langley* the defendants wanted to buy farm property on which Planters Bank had several defaulted notes. The Bank provided financing for the purchase of the farm and the defendants in turn signed a promissory note, mortgage, and personal guaranties in favor of Planters Bank. These documents contained unconditional promises to pay.

However the Langleys did not pay and were subsequently sued by the Bank. In response the Langleys filed suit against the bank and other parties alleging that the bank

had made various representations to persuade the Langleys to buy the property and that these representations were not true. The Langleys maintained that these misrepresentations relieved them of their obligation to pay on the note.

It was undisputed that the representations were not contained in any part of the documents on which the Langleys were obligated to pay. During the course of the suit the Bank was declared insolvent and the FDIC intervened in the lawsuit. The FDIC moved for summary judgment. The district court granted the motion, holding that section 1823(e) precluded the Langleys' defense. The Langleys appealed, contending that two representations, involving the acreage of the farm and mineral rights, when considered separately, were outside of section 1823(e) and could be asserted against the FDIC.

The Fifth Circuit affirmed the district court, holding that the attempts by the Langleys to assert the misrepresentations against the FDIC was an attempt to vary the terms of the documents held by the FDIC. The Court noted:

> [i]n the instant case, the Langleys and Planters did enter into a side arrangement which was not disclosed in the loan papers. Moreover the Langleys attempt to rely on various parts of that undisclosed arrangement to vary and add terms to the loan documents they executed. The Langley/Planters' undisclosed side agreement involved not only promises regarding the borrowing of money but also the bank's furnishing the property to be bought with the loan proceeds. As part of this undisclosed arrangements. Planters made certain misrepresentations regarding the loan terms (e.g. nonrecourse nature of the loan) and the property to be purchased (e.g., surface and mineral acreage). Despite the critical importance of these oral warranties, they were not disclosed in the executed loan documents (nor do these documents indicate that Planters was so involved in the land purchase).

> Thus, to allow the Langleys to shift the focus of their defense in the instant case would create an unacceptable "end run around section 1823(e)." *Langley,* 792 F.2d at 546 (citation omitted).

In this case the Defendant, Rex Huston, is also attempting to vary the terms of the written documents. The precondition arrangement is not disclosed in the note or in the guaranties.

Defendant argues however that he is not attempting to enforce any side agreement against the FDIC, the agreement in itself is a defense to the FDIC's claims. Defendant however is asserting the same argument that the Langleys did. The Langleys were not attempting to enforce the arrangement they had with Planters Bank. They were also just trying to assert that the agreement or representations made the note unenforceable against them. Basically both Defendants, Rex Huston and the Langleys, claim that the agreement relieves them of their obligation just by its mere existence and thus is not precluded from being asserted against the FDIC. The Fifth Circuit rejected such an argument and the Supreme Court affirmed.

Thus the Court finds that the arrangement between the Bank and Defendant was an agreement which tends to diminish the rights of the FDIC, the statutory protection applies and Defendant cannot use the agreement against the FDIC.[4]

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[4] The Court notes that at the offset this conclusion seems contradictory to the conclusion contained in Section A, 2. In the instant case the agreement has been turned into a double-edged sword. Defendant cannot use it to establish usury, but the FDIC can use it to establish consideration. However the existence of the agreement is not being disputed, just the assertion of it *against* the FDIC.

B. DEFENDANT'S CLAIMS FOR AFFIRMATIVE RELIEF AGAINST THE FDIC.

Defendant claims that he is entitled to all statutory relief relating to usurious claims, that is, he is entitled to three times the usurious interest charged and attorney's fees. Defendant brings this claim against the FDIC in both capacities.

Defendant claims that the precondition impose by the bank, the signing of the guaranties, on his receipt of a loan, was, under Texas law, interest on the $110,000.00 note. These guaranties plus the interest on the face of the note rendered the interest rate over 100%, a usurious rate.

This Court has already determined that this arrangement was an agreement in violation of section 1823(e). *See* section A.3, *supra.* However this section is not applicable in proceeding where the FDIC is acting in its receivership capacity. *Federal Deposit Insurance Corporation v. McClanahan,* 795 F.2d 512, 514 and 516 (5th Cir. 1986).

But the federal common law as announced in *D'Oench, Duhme & Co. v. Federal Deposit Ins. Corp.*, 315 U.S. 447 (1942) is applicable to proceedings in which the FDIC is acting in either or both of its capacities.[5] *D'Oench* has been cited for the proposition that secret agreements cannot be used as a defense to recovery by the FDIC. *McClanahan,* 795 F.2d at 517. In this instance Defendant is using the agreement offensively to diminish the FDIC's recovery on the notes and guaranties. However the use of the secret agreement also violates the principle of *D'Oench, Duhme.*

In *D'Oench, Duhme,* suit was brought by the FDIC to recover payment on certain notes, the Defendant responded alleging that the notes had been given to the bank without consideration. The bank had purchased various bonds from Defendant. Later the bonds defaulted. The bank and Defendant then entered into an agreement whereby certain notes were executed so that the Bank could carry the notes and not show any past due bonds. Defendant

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[5] *See McClanahan,* 795 F.2d at 514, n.1., and at 516 (applying *D'Oench* when the FDIC was suing in its receivership capacity) and *FDIC v. Cardinal Oil Well Servicing Co., Inc.*, 837 F.2d 1369, 1372 (5th Cir. 1988) (*D'Oench* prevented the assertion of the defense of misrepresentation against the FDIC suing in its corporate capacity).

obtained a receipt for the notes which contained the following language: "[T]his note is given with the understanding it will not be called for payment. All interest payments to be repaid."

Subsequently the Bank was declared insolvent and the FDIC acquired the notes and brought suit for payment. The defendant produced the receipt asserting the defense of no consideration for the notes.

The Supreme Court held that the Defendant was estopped from asserting this defense because "an accommodation maker is not allowed that defense as against the receiver of the bank and its creditors, or at times even as against the bank itself, where his act contravenes a general policy to protect the institution of banking from such secret agreements." *D'Oench, Duhme,* 315 U.S. at 458. The Court also held that because of the general policy "the defendant could not rely on his own wrongful act to defeat the obligation of the note as against the receiver of the bank." *Id.* at 457-58.[6]

Thus if Defendant Rex Huston was allowed to assert his side arrangement as a basis for his counterclaim against the FDIC in either or both capacities he would be "rely[ing] on his own wrongful act to defeat the obligation of the note as against the receiver of the bank."[7]

The Texas usury statute, Tex. Rev. Civ. Stat. Ann. art. 5069-1.02 (Vernon 1987), provides that:

> (1) Any person who contracts for, charges or receives interest which greater than the amount authorized by

[6] The court was applying the general policy embodied in the National Banking Act and as explained in *Detrick v. Greaney,* 309 U.S. 190 (1940).

[7] Defendant would be defeating the obligation since in his own brief he admits that he intends to seek an offset on the notes and guaranties which would effectively eviscerate any recovery the FDIC would have on the notes and guaranties. The Court is aware that the FDIC in its receivership capacity no longer has the notes, however Defendant's claims are aimed against FDIC in its corporate capacity. The FDIC in its receivership capacity is being sued only as stepping stone to obtain relief from the FDIC in its corporate capacity. Further the FDIC in its receivership capacities, according to Defendant no longer has any assets of the bank to pay for any liabilities asserted against it.

> this Subtitle, shall forfeit to the obligor three times the amount of usurious interest contracted for, charged or received,...and reasonable attorney fees fixed by the court...
>
> (2) Any person who contracts for, charges or receives interest which is in excess of double the amount of interest allowed by this Subtitle shall forfeit as an additional penalty, all principal as well as interest and all other charges and shall pay reasonable attorney fees....

Thus if the Defendant is allowed to assert his usury counterclaim and he proves his claim, then the FDIC's recovery on the notes and guaranties would be substantially less.[8]

Plaintiff argues that "the primary rationale supporting *D'Oench* Doctrine is that it allows bank regulatory agencies to rely on the integrity of a bank's books and records." *FDIC's Reply Memorandum of Law,* at 28. *D'Oench, Duhme* applies when the Defendant has "lent himself to a scheme or arrangement whereby the (appropriate) banking authority ...was or was likely to be misled." 315 U.S. at 460 (cited in *McClanahan* 795 F.2d at 517). Thus a defendant is estopped from asserting a secret agreement which alters the bank records because "it (the defendant) was responsible for the creation of the false status of the note in the hands of the bank." 315 U.S. at 461.

This rationale was applied to estop a defendant who was so "responsible" from asserting a counterclaim against the FDIC. *Federal Deposit Ins. Corp. v. Chessen,* No. 83-2476 (D. Kan. Oct. 2, 1986) (LEXIS, Genfed library, Dist. file). In *Chessen* the Defendant had signed two notes in favor of ISSB, a bank in Kansas. The notes were signed with the understanding that the Defendant would not be personally liable for the notes and that the notes would be "rolled-over" for up to three years. The notes had been executed at

[8] Defendant is asserting that under *First Empire Bank v. Federal Deposit Ins. Corp.,* 572 F.2d 1361 (9th Cir.), *cert. denied,* 439 U.S. 919 (1978), he can offset the usurious interest against the FDIC in its corporate capacity.

the urging of a group of individuals that sought additional financing for their real estate business. Defendant used the proceeds from the notes to acquire an interest in two limited partnerships established by that group.

The bank was declared insolvent and the FDIC as receiver became the owner of the bank's assets and liabilities. The FDIC brought suit to collect on the notes executed by Defendant, which were in default. The Defendant asserted various defenses and later sought to add five counterclaims. The court refused to allow him to file the counterclaims, holding that the *D'Oench* rule prohibited a defendant, who had lent himself to a scheme that would tend to mislead the banking authorities, from asserting either affirmative defenses or counterclaim which arise out of the deceptive scheme.

This Court agrees with that rationale. A defendant cannot benefit from his own wrongful actions. Here Defendant Rex Huston agreed to enter into a scheme that could deceive the bank examiners and indeed was intended to so deceive. *See* Deposition of Rex Huston at 34 ("the guarantees would stay blank and that the only reason that he wanted them was for the regulators,....."), and now he requests damages arising from his participation in that scheme.

Therefore the Court finds that under the general policy of protecting the FDIC from secret agreements so that it may rely on bank records in appraising the worth and collectibility of the bank's assets,[9] the Defendant cannot assert his counterclaim for usury against the FDIC in either capacity. Defendant was responsible for the creation of the false status of the note and guaranties in the bank records.[10]

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[9] *See Castle*, 781 F.2d at 1108, n.3 (noting "the import-policy considerations discussed by the *Powers* court").

[10] Defendant does not suggest that he was unaware of the deception and as the Supreme Court noted in *D'Oench*, "[p]lainly one who gives such a note to a bank with agreement that it will not be enforced must be presumming that it will conceal the truth from the vigilant eyes of bank examiners." 315 U.S. at 460.

CONCLUSION:

Plaintiff's Motion is granted in all respects except on the question of damages. Plaintiff shall prepare a proposed judgment based upon the amounts requested in Plaintiff's original petition.

It is SO ORDERED.

Entered this 22nd day of August, 1988.

MARY LOU ROBINSON

MARY LOU ROBINSON
UNITED STATES
DISTRICT JUDGE